Supreme Court, U. S.
FILED
MAY 29 1979
MICHAEL RODAK, JR., CLERK

PETITION

IN THE

Supreme Court of the United States

October Term, 1978

No. 78-1775

JOSEPH A. SCHAFER, WHITNEY W. IRONS, ALTON P. GAINER, EMIL MILAN, CAROL KUCHAR, LEO SUKALA, STEPHEN SLOBODA and CHARLES W. HANNON, Stockholders of Penn Central Company,

Petitioners,

v.

PENN CENTRAL CORPORATION, formerly PENN CENTRAL TRANSPORTATION COMPANY, PENN CENTRAL COMPANY and THE UNITED STATES OF AMERICA,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT AT NOS. 78-1715, 78-2321 AND 78-2336.

PETITION FOR A WRIT OF CERTIORARI

CLETUS P. LYMAN
RICHARD A. ASH
Attorneys for Petitioners

LYMAN & ASH
1612 Latimer Street
Philadelphia, PA 19103
(215) 732-7040

This petition is related to a petition being filed at the same time, *Dr. Robin S. Key, etc., v. Penn Central Corporation, etc., et al.*

BATAVIA TIMES APPELLATE COURT PRINTERS
EDWARD W. SHANNON
EASTERN PENNSYLVANIA REPRESENTATIVE
THE PLAZA, SUITE 23F, PHILADELPHIA, PA. 19103
PHONE: (215) 568-7788

INDEX.

	Page
Opinions and Judgments Below	2
Jurisdiction	5
Constitutional and Statutory Provisions Involved	5
Statement of Questions Presented for Review	5
Statement of the Case	6
1. Nature of the Proceedings	6
2. Statement of Facts and Prior Proceedings	7
Reasons Why The Writ Should Be Allowed	16
1. The Court of Appeals sanctioned conduct by the District Court which was contrary to due process of law, as interpreted by this court	16
2. This court should take final responsibility in a matter involving the property rights of approximately 150,000 citizens where there is at least the appearance that the government is responsible for ruinous losses	17
3. This court should remedy a great injustice to railroad stockholders	18
Conclusion	20
Test of Constitutional and Statutory Provisions Involved	21
Amendment V The Constitution of the United States	21
Section 77, Bankruptcy Act	21
Sections of the Pennsylvania Business Corporation Law, 15 P.S. §§ 1311 and 2102	21

Page

TABLE OF AUTHORITIES.

Cases:

In Re Penn Central Transportation Company, 355 F. Supp. 1343 (E.D.Pa. 1973) 8

In re Valuation Proceedings, etc., 445 F. Supp. 994 (Special Court 1977) 14

Mullane, Special Guardian v. Central Hanover Bank and Trust Company, 339 U.S. 306 (1950) 16,17

Regional Rail Reorganization Act Cases, 419 U.S. 102 (1974) 8,9,18

Statutes:

Bankruptcy Act:

Chapter X, 11 U.S.C. § 501 *et seq.* 4,5

Chapter XI, 11 U.S.C. § 701 *et seq.* 2,5,7,12,14

Section 77, 11 U.S.C. § 205 5,7,8

Pennsylvania Business Corporation Law, 15 P.S. §§ 1311(B), 1320(1) and 2102 5,17

Regional Rail Reorganization Act of 1973 6,8

Title 28 U.S.C. § 1254(1) 5

Tucker Act, 28 U.S.C. § 1491 8,18

45 U.S.C. § 701 8,11

45 U.S.C. § 716 11

Constitution:

Amendment V of the Constitution of the United States 5

IN THE

Supreme Court of the United States

October Term, 1978

No. .....

JOSEPH A. SCHAFER, WHITNEY W. IRONS, ALTON P. GAINER, EMIL MILAN, CAROL KUCHAR, LEO SUKALA, STEPHEN SLOBODA and CHARLES W. HANNON, Stockholders of Penn Central Company,

Petitioners,

v.

PENN CENTRAL CORPORATION, formerly PENN CENTRAL TRANSPORTATION COMPANY, PENN CENTRAL COMPANY and THE UNITED STATES OF AMERICA,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Petitioners, Joseph A. Schafer, Whitney W. Irons, Alton P. Gainer, Emil Milan, Carol Kuchar, Leo Sukala, Stephen Sloboda and Charles W. Hannon, stockholders of Penn Central Company, pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, rendered in these proceedings on January 11, 1979 (12a*), affirming orders of the United States District Court

* This refers to page 12 of the appendix to this petition, printed separately. The appendix is also the appendix to the petition of Dr. Robin S. Key.

for the Eastern District of Pennsylvania, and an order (10a) entered on the same date dismissing other appeals from the District Court.

Opinions and Judgments Below

The District Court entered an order on August 16, 1976, continuing Penn Central Company (referred to hereinafter as "the holding company" and sometimes referred to in the lower courts as "PCC") in possession under Chapter XI of the Bankruptcy Act, 11 U.S.C. § 701 *et seq.*, without opinion. A copy of the order is reproduced in the appendix at pages 217a-221a. The District Court entered an order approving the plan of reorganization of Penn Central Transportation Company ("PCTC" or "the railroad") on March 17, 1978, with opinion. The order and the parts of the opinion relating to petitioners are printed in the appendix at pages 134a-216a and the opinion is reported at 358 F.Supp. 1234 (E.D.Pa. 1978). A District Court bankruptcy judge entered an order on April 21, 1978, authorizing the holding company, as sole stockholder of the railroad, to vote in favor of the amended plan of reorganization filed by the trustees for PCTC, without opinion. The order is printed in the appendix at 133a.

The bankruptcy judge entered an order on August 3, 1978, for petitioners to show cause why a motion of the holding company for summary judgment dismissing petitioners' adversary complaint should not be granted, without opinion. The order is printed in the appendix at 132a. The bankruptcy judge denied motions of petitioners for a continuance and for leave to take discovery and granted the holding company's motion for summary judgment at a hearing on August 16, 1978. The part of the transcript, deciding these motions, is printed in the appendix at 131a.

The District Court entered an order confirming the railroad plan of reorganization and an order directing that the plan be consummated on August 17, 1978, with opinion. The confirmation order is printed in the appendix at 99a-106a; the consummation order is printed in the appendix at 49a-98a; and, the part of the opinion relating to petitioners is printed in the appendix at 107a-130a and is reported at 458 F.Supp. 1364 (E.D.Pa. 1978). The bankruptcy judge entered an order confirming the plan of arrangement of the holding company under Chapter XI on August 21, 1978, without opinion. The order is reproduced in the appendix at 46a-48a. The District Court entered an order affirming the order of the bankruptcy judge granting summary judgment dismissing the adversary complaint on October 10, 1978, without opinion. The order is printed in the appendix at 45a. The District Court entered an order affirming the order of the bankruptcy judge, confirming the plan of arrangement of the holding company on October 12, 1978, without opinion. The order is printed in the appendix at 44a.

The Court of Appeals entered an order on October 17, 1978, denying a motion by petitioners for a stay of consummation of the railroad plan of reorganization and the holding company plan of arrangement, without opinion. The order is printed in the appendix at 42a-43a. Associate Justice William J. Brennan, Jr., of this court, denied a similar application for a stay on October 23, 1978, without opinion. A copy of a letter from the clerk of this court, advising of this endorsement, is printed in the appendix at 41a. This court denied the same application, after it was readdressed to the Chief Justice and referred to the court, on November 13, 1978. A letter from the clerk advising of the entry of this order is printed in the appendix at 40a.

The bankruptcy judge entered an order on December 12, 1978, dismissing an adversary complaint filed by Dr. Robin S. Key and denied the motion of Dr. Key to have the Chapter XI case proceed under Chapter X of the Bankruptcy Act, with opinion. The order and opinion are printed in the appendix at 37a-39a, and the opinion is unreported.

The Court of Appeals entered judgment affirming the orders of the District Court, filed October 10, 1978, and October 12, 1978, and entered an order dismissing appeals from orders of the District Court dated March 17 1978, and August 17, 1978, with opinion. The judgment is printed in the appendix at 11a-12a; the order, at 9a-10a; and the opinion at 13a-36a. The opinion is not yet reported. The Court of Appeals entered an order on January 15, 1979, dismissing appeals taken by Dr. Key from the orders of the District Court of March 17, 1978, and August 17, 1978, without opinion, referring to its opinion of January 11, 1979. The order is printed in the appendix at 8a.

The Court of Appeals entered an order on February 8, 1979, amending its opinion of January 11, 1979. A copy of the order is printed in the appendix at 6a-7a.

The District Court entered an order on February 27, 1979, affirming the order of the bankruptcy judge, entered December 12, 1978, without opinion. The order is printed in the appendix at 4a-5a.

The Court of Appeals entered an order on February 28, 1979, denying a petition for rehearing, without opinion. The order is printed in the appendix at 3a-4a. The Court of Appeals entered an order on March 1, 1979, amending its opinion of January 11, 1979. The order is printed in the appendix at 1a-2a.

Jurisdiction

The Court of Appeals entered judgment, affirming orders of the District Court on January 11, 1979. On the same date, the Court of Appeals dismissed appeals from other orders. Petitioners filed a timely petition for rehearing on January 25, 1979, which was denied by order of February 28, 1979 (3a-4a).

The jurisdiction of this court is invoked under Title 28 U.S.C. § 1254(1), granting jurisdiction to this court to review cases in the courts of appeals by writ of certiorari before or after rendition of judgment.

Constitutional and Statutory Provisions Involved

This case involves Amendment V of the Constitution of the United States; Section 77 of the Bankruptcy Act, 11 U.S.C. § 205; Chapter X of the Bankruptcy Act, 11 U.S.C. § 501 *et seq.*; Chapter XI of the Bankruptcy Act, 11 U.S.C. § 701 *et seq.*; and the Pennsylvania Business Corporation Law, 15 P.S. §§ 1311(B), 1320(1) and 2102. The texts of relevant parts of these constitutional and statutory provisions are printed at the end of this petition.

Statement of Questions Presented for Review

1. May a District Court, by a series of actions in interdependent bankruptcy proceedings involving a railroad, adopt plans of reorganization and arrangement that reduce the equity interests of the 150,000 stockholders of the holding company without providing either for individual, mailed notice to the stockholders of their right to be heard and to contest such plans in court or for a stockholders meeting to consider such plans and to empower representatives to carry out the will of the stockholders in court?

2. Do stockholders of a holding company have a right to be heard and to appeal orders adopting a plan of reorganization of a railroad?

3. May a District Court reorganize the interests of creditors and stockholders of a railroad and its holding company without making a finding as to the value of their estates?

4. Were the 150,000 stockholders of Penn Central Company entitled to only four percent of the common stock of Penn Central Corporation, the corporation that emerged from the bankruptcy proceedings, where the new corporation has a multibillion dollar claim against the United States and other valuable assets?

5. Should directors nominated by creditors be given power to settle a claim which, if litigated, could result in great benefit to stockholders?

6. Do the plans of reorganization and arrangement of the railroad and its holding company, together with the provisions of the Regional Rail Reorganization Act of 1973, constitute an overall unconstitutional taking of the property of the stockholders of the holding company by the United States?

Statement of the Case

1. Nature of the Proceedings.

These are two proceedings in bankruptcy. One is a proceeding for the reorganization of a railroad and the other is a Chapter XI proceeding for arrangement of the railroad's holding company. Petitioners are eight stockholders of the holding company.*

* A ninth stockholder, Dr. Robin S. Key, is filing a separate petition, incorporating this petition by reference.

Petitioners complain that, although they owned the equity interest in an immensely valuable railroad before bankruptcy, the courts below have arbitrarily allocated them only a four percent interest in the reorganized corporation and have done so without providing stockholders an opportunity to learn of the proceedings, to be heard, to vote on the plans, or to appeal from orders approving and confirming the plan of reorganization of the railroad and providing that it be consummated.

Jurisdiction of the District Court was invoked under Section 77 and Chapter XI of the Bankruptcy Act.

2. Statement of Facts and Prior Proceedings

Approximately 150,000 stockholders own approximately 24 million shares of the holding company. By a series of steps in two interdependent bankruptcy proceedings, these stockholders have had their interests reduced to only four percent of the equity of the emerging public company, Penn Central Corporation. They are being required to turn in 25 shares for one new share. Creditors of the holding company are receiving six percent of the equity, and creditors of the railroad, ninety percent.

The lower courts held that the stockholders had no right to participate in the proceedings resulting in this alteration of their interests and the stockholders have never received individual, written notice of an opportunity to be heard and contest such alteration.

As of December 31, 1969, the total assets of the holding company were $6.851 billion and the net worth was $2.810 billion, or, a book value per share of approximately $117. In 1969, PCTC operated the Penn Central Railroad and held large amounts of real estate.

On June 21, 1970, PCTC filed for reorganization under Section 77 of the Bankruptcy Act, providing for the rehabilitation of railroad debtors. 11 U.S.C. § 205. On February 10, 1971, the railroad trustees reported to the District Court that PCTC was not viable under existing regulatory constraints. On March 6, 1973, the District Court filed a memorandum concluding that it was highly doubtful that the railroad could properly be permitted to continue to operate. *In Re Penn Central Transportation Company,* 355 F.Supp. 1343, 1345-6 (E.D.Pa. 1973). In July, 1973, the trustees submitted a plan of reorganization, which contemplated termination of all rail operations and liquidation of all rail properties unless arrangements were made with public authorities to assume interim losses.

On January 2, 1974, the Regional Rail Reorganization Act of 1973 ("RRRA") became law. 45 U.S.C. § 701 *et seq.* RRRA provided that the railroad operate under the aegis of the lower court for a further period, approximately 20 months, during which time the United States Railway Association ("USRA"), a new corporate entity created under the act, would complete the task of planning a new rail system or systems, and deciding what portions of the bankrupt's rail facilities should be conveyed to Consolidated Rail Corporation ("ConRail"), the company which was to take over the system which USRA designed. ConRail was to pay PCTC in securities.

In 1974, a constitutional challenge to RRRA resulted in a decision by this court, that RRRA, as supplemented by the Tucker Act, 28 U.S.C. § 1491, was constitutional. *Regional Rail Reorganization Act Cases,* 419 U.S. 102 (1974). The Tucker Act provides for money damages against the United States.

On April 1, 1976, PCTC's railroad properties were conveyed to ConRail.

As the consequence of all of this, the PCTC estate consisted of real estate and other investments not acquired by ConRail, plus PCTC's claims under RRRA and the Tucker Act, against ConRail and the United States.

The assets remaining on hand were valued by the lower court at almost $1.85 billion, not including the value of the claim against ConRail and the United States. The claims are currently in litigation in a special court established by RRRA for the express purpose of handling these claims. This litigation is called "the Valuation Case." The principal amount of all claims against the estate, before reorganization, totaled more than $3 billion, with interest, as of 1978.

The District Court did not place a value on the Valuation Case. To the contrary, the District Court said that it did not wish to take evidence on this point. The Securities and Exchange Commission ("SEC") staff evaluated the proceeds of the Valuation Case as possibly ranging between $500 million and $11 billion as of 1976. The proceeds are subject to eight percent annual interest. Mr. Justice Douglas described the value as "unknown billions—perhaps 10 or 12 billion" in *Regional Rail Reorganization Act Cases, supra,* 419 U.S. at 180.

On September 20, 1977, the SEC staff reported to the District Court:

> "The expectation of a large recovery from the Valuation Case is not a matter of contingency or unfounded hope. It is as certain as any future event can be."

The Valuation Case involves two separate issues: (1) the "conveyance taking issue" relating to just compensation for the properties conveyed by PCTC to ConRail on April 1, 1976, and (2) the "erosion taking issue" relating to losses

sustained when PCTC operated a railroad involuntarily. The book value of the property conveyed to ConRail by PCTC was about $3.2 billion. PCTC experienced net railway operating losses from 1970 through 1976 before fixed charges, of $900 million, plus another $400 million of extraordinary loss items, mostly rail related.

The Valuation Case is expected to take until 1987 for completion. This court has appellate jurisdiction to review decisions of the special court. Taking the high valuation, the recovery from the case could be over $20 billion, with interest. Under the plan of reorganization, almost all of this would go to the former creditors of PCTC in exchange for slightly over $3 billion in claims. This would be a great windfall to creditors and a corresponding shortfall to stockholders.

Other assets of PCTC received cursory consideration in the lower courts, leading to the unreasonably low equity assigned to stockholders. For example, the SEC concluded that coal reserves in the amount of 1.2 billion tons would be worth only $111 million as of the end of 1982. The District adopted the SEC report in this respect. There was little justification for this remarkably low value (less than 10 cents per ton). Petitioners could have provided expert testimony that coal reserves are now worth from 25 cents to $5 per ton.

The District Court ignored the possibility that the stock of ConRail, to which PCTC was entitled under RRRA, may have great value in the future. This was to be the primary form of compensation to PCTC for conveyance of rail assets on April 1, 1976, and is exclusive of opportunities to obtain other securities and cash in the Valuation Case.

The District Court made no effort to independently value the securities even though ConRail operates the principal rail

network in the Northeastern United States. The District Court said that it assumed that the ConRail securities "will be valueless." This is contrary to the expressed intent of Congress in enabling legislation that ConRail be financially self-sustaining (45 U.S.C. § 716) and that it be able to attract additional private investment (45 U.S.C. § 701).

The District Court also overlooked the value of the combined tax loss carry forward of the companies, amounting to over $1 billion.

The District Court approved the appointment of nominees of creditors to the initial board of directors of the reorganized company (one director is the lawyer who represented the creditors of the holding company in the Chapter XI proceedings). The stockholders received no representative on the board. This board was also given the power to settle the Valuation Case.

The stockholders of the holding company were excluded from participation in formulating the plans by a series of legal maneuvers.

In 1969, when bankruptcy was foreseeable to management of the railroad, the board of directors distributed proxy material to the stockholders of the railroad, which was then directly owned by public investors. The directors proposed that stockholders exchange their stock, one for one, for the common stock of a holding company. The stated reasons for the reorganization were that management had embarked on a program of diversification. Management had several possible acquisition prospects in mind. Management believed that the stock of a holding company would provide greater flexibility in this program. The investing public identified the securities of the railroad with railroad transportation. The issuance of securities by a railroad required prior approval of the In-

terstate Commerce Commission. Restrictions applicable to the issuance of securities by a railroad would make it difficult for the company to carry out a diversification program. A holding company pattern would expedite and facilitate the merger of various railroad subsidiaries.

The truth of the matter was that diversification was impossible because the railroad was moving into debt amid mounting operating losses. The significance of the holding company was to cloud the standing of the stockholders in the forthcoming railroad bankruptcy proceedings, filed on June 21, 1970.

The District Court treated the holding company rather than its stockholders as the only party having an equity interest in the railroad. The holding company continued to operate without court protection until July 22, 1976, when it filed a petition for arrangement under Chapter XI of the Bankruptcy Act. However, it stopped holding stockholder meetings in 1974 because management deemed them too expensive. On August 16, 1976, a petition to continue as debtor in possession was granted (217a-221a).

The seven directors of the holding company, six of whom were elected at the last stockholders meeting in 1974, and one of whom was appointed on May 21, 1975, by the other six, acted during the critical final years of the railroad's reorganization as if they were the ultimate equity owners. The Chapter XI bankruptcy court accorded counsel selected by the directors full authority to bind the holding company. At a hearing on May 28, 1977, the bankruptcy court directed the holding company to file a consent to the plan of reorganization of PCTC. Counsel for the holding company asked the court to enter the order. The District Court having jurisdiction over the railroad reorganization relied heavily on the support of the holding company in approving the railroad plan of reorganization (213a).

On April 21, 1978, counsel selected by the 1974 directors applied to the bankruptcy court for an order authorizing the holding company to vote in favor of the railroad plan of reorganization. The bankruptcy court entered an order granting the petition the same day (133a). At no time did the stockholders of the holding company receive notice of the proceedings under Chapter XI. They were given no opportunity to be heard on the questions whether the holding company should declare its support of the railroad plan of reorganization, in 1977, or whether the holding company should vote for the plan of reorganization, as finally approved, in the spring of 1978. The holding company failed to hold stockholder meetings after 1974 and never held a meeting for the purpose of considering the PCTC plan of reorganization.

Petitioners here and Dr. Key, who is filing a related petition, collectively hold about 240,000 shares of the holding company stock. Dr. Key and Mr. Sukala hold about 100,000 shares each. They learned about the plan to reorganize the railroad through newspaper accounts at times ranging from when the plan was first filed with the court in 1977, in the case of Mr. Schafer, to several months after the plan was approved, in the case of Dr. Key. Petitioners here first engaged counsel in April, 1978, after the District Court approved the plan and when they first recognized that their equity interests had been disastrously reduced. (Dr. Key first hired counsel on July 19, 1978.) Petitioners filed a timely appeal from the approval of the plan as well as from its confirmation and an order providing for consummation.

After petitioners' counsel reviewed what had already taken place in the two proceedings, he appeared at the hearing of July 27, 1978, to oppose confirmation. On the same date, petitioners filed an adversary proceeding before the Bank-

ruptcy judge in the Chapter XI court to set aside declarations of support for the plan by the holding company, the vote in favor of the plan by the holding company as sole stockholder, and to require a meeting of holding company stockholders. Petitioners raised the *ultra vires* character of what the holding company was purporting to do as a collateral attack in the railroad proceeding.

The district judge in the railroad proceeding took the position that stockholders of the holding company had no standing to oppose confirmation (116a). In the Chapter XI proceeding, the bankruptcy judge took the position that stockholders lacked standing because Chapter XI is designed only to modify or alter the rights of unsecured creditors and no provision of the act permits a plan, proposed under Chapter XI, to deal with the rights of stockholders (39a).

The district judge overseeing the railroad reorganization reviewed a decision of the special court (*In re Valuation Proceedings, etc.*, 445 F.Supp. 994, 1031 (Special Court 1977)), and concluded that valuation theories which would generate an award approaching 11 billion 1976 dollars had been rejected (117a). The District Court failed to note that the special court also characterized as "incredible" an initial offer of only $506.5 million. 445 F.Supp. at 1029. The district judge found the railroad reorganization plan equitable to holding company stockholders in spite of petitioners' objections (121a).

The bankruptcy judge summarily dismissed petitioners' adversary complaint and objections to the holding company plan of arrangement, apparently on the basis that stockholders had no standing to participate (131a). His orders were summarily affirmed by the supervising district judge on October 10 and 12, 1978 (44a-45a). The reason for affirming

without opinion was probably the stated desire of the parties to proceed quickly to the Court of Appeals, where a hearing had been scheduled for October 16, 1978, on appeals from approval and confirmation of the railroad reorganization plan, scheduled to be consummated on October 24.

On October 17, 1978, the Court of Appeals denied petitioners' motion for a stay of consummation of the railroad plan of reorganization and the holding company plan of arrangement, pending appeal (42a-43a). On October 23, 1978, Mr. Justice Brennan denied a stay application to the same effect (41a), and on November 13, 1978, this court denied the same stay application referred to it by the Chief Justice (40a).

The plans were consummated on October 24, 1978, as scheduled. On January 11, 1979, the Court of Appeals handed down its decision, dismissing stockholder appeals from the railroad reorganization plan on the ground of lack of standing and affirming the actions of the bankruptcy judge in the Chapter XI proceeding. However, the Court of Appeals said:

> "Because of the importance of this matter and the potentially devastating consequences of unnecessary delay, however, we deem it advisable to discuss the merits of appellants' claims so as to reduce the likelihood of a remand to this court should the Supreme Court decide that we have erred in dismissing these appeals (22a)."

The Court of Appeals reviewed the uncertainty of the value of equity interests, praised the extraordinary job done by the railroad reorganization judge, conceded that granting a contingent interest in the Valuation Case to holding company shareholders could perhaps have been approved on appeal, but decided that a plan which gives holding company stockholders a small present interest is fair. The Court of Appeals agreed that stockholder participation was not required

under Chapter XI proceedings because, "an arrangement under Chapter XI may not deal with the rights of shareholders (34a-35a)." The Court of Appeals ignored that the Chapter XI court had, in fact, dealt with shareholder rights by both authorizing the holding company's agreement to the railroad plan of reorganization and by dividing the equity interest assigned thereunder to the holding company, 60:40, between the holding company's creditors and its stockholders.

REASONS WHY WRIT SHOULD BE ALLOWED

1. The Court of Appeals sanctioned conduct by the District Court which was contrary to due process of law, as interpreted by this court.

The Court of Appeals approved of the exclusion of approximately 150,000 Penn Central stockholders from participation in proceedings which drastically altered and reduced the value of their property interests. The Court of Appeals itself held that stockholders lacked standing to appeal critical orders affecting their interests. In *Mullane, Special Guardian v. Central Hanover Bank and Trust Company,* 339 U.S. 306 (1950), this court held that courts may not decide important questions affecting property interests without individual, mailed notice to affected parties of their right to be heard and contest such judicial action. The Court of Appeals overlooked the fundamental unconstitutionality of such exclusion by taking a step by step approach in its analysis. The court said:

> "If, however, both the reorganization plan and the arrangement meet the requirements of Section 77 and Chapter XI respectively, no such constitutional violation (of the right to due process) would exist (30a-31a)."

To the contrary, fidelity to the literal provisions of the Bankruptcy Act does not guarantee constitutional sufficiency. "Due process" requires that petitioners be given an opportunity and notice to be heard at every meaningful state in consideration of the approval of the plans of reorganization and arrangement.

The Court of Appeals relied on a provision of the Pennsylvania Business Corporation Law, 15 P.S. § 1320(1), in holding that the bankruptcy judge could authorize the holding company to support and vote in favor of the railroad reorganization plan and confirm the holding company plan. The statute provides that approval by stockholders may be omitted if corporate action in question is authorized by a bankruptcy judge. This Pennsylvania statute does not and constitutionally cannot give federal bankruptcy courts the power to act without *Mullane* notice to stockholders before approving corporate action, which ordinarily would require a favorable vote of the stockholders and which disastrously alters their property interests.

2. This court should take final responsibility in a matter involving the property rights of approximately 150,000 citizens where there is at least the appearance that the government is responsible for ruinous losses.

The railroad had a net worth of $2.810 billion when it went into reorganization. There was good ground to believe the net worth was understated because of the enormous market value of the railroad's real estate holdings, which many believed to have been conservatively stated. This net worth belonged to 150,000 public investors, many of them small stockholders who had invested a large portion of their life savings. The government took responsibility to see that the stockholders get their fair share in two senses. Under the Bankruptcy Act, the federal courts have taken the estate of the railroad for

purposes of reorganization and interim administration. Congress required interim operations at a loss and conveyance of the properties deemed necessary to continue the operation of a railroad, to ConRail.

The stockholders are getting only nominal value at the end of the reorganization. They feel that they have been dealt with unfairly. Even if the stockholders were entitled to only four percent of the reorganized corporation, this court should give the stockholders a hearing so that, by its prestige, it may help put to rest suspicion that the government has cheated the stockholders. This is particularly true because of the holdings of the lower courts that stockholders were to be excluded, while according full standing to governmental parties, banks, insurance companies and other large institutions.

3. This court should remedy a great injustice to railroad stockholders.

In *Regional Rail Reorganization Act Cases, supra,* this court enforced the provisions of the Fifth Amendment requiring that the government provide just compensation for property taken, by authorizing a Tucker Act remedy for money damages against the United States. The lower courts, in approving the plans of reorganization and arrangement, have diverted this remedy from the stockholders to former creditors of the railroad and its holding company. The provisions of RRRA requiring conveyance of railroad properties to ConRail and requiring the railroad to operate while losing money made it impossible for the railroad holding company to raise enough money to pay its creditors by 1978.

The railroad as of 1978 had $1.85 billion in assets able to be turned to cash, (allowing reasonable time to liquidate some assets). Its liabilities were about $3 billion. The rail-related losses during bankruptcy alone were about equal to the shortfall. In other words, if the railroad had not operated during bankruptcy, it would have had enough cash to pay its creditors and the claim against the United States for conveyance of the railroad to ConRail would belong exclusively to the stockholders.

The combined effects of RRRA and the actions of the bankruptcy court are to place all of the burdens of the time and uncertainty of establishing the liability of the government to the railroad upon the stockholders. Although the District Court recognized the existence of the Valuation Case, it gave it very little weight in allocating shares of the reorganized company because the amount of the ultimate proceeds are unknown.

By mandating conveyance of the railroad assets as of 1976, the United States prevented the railroad from selling its property to raise cash to pay its debts. Since RRRA has deferred compensation to the railroad until valuation can be completed in 1987, the lower courts should have provided that stockholders, by a special class of securities, receive the proceeds of the Valuation Case in excess of what is needed to fully pay the claims of creditors.

The District Court put the creditors in control of the settlement of the Valuation Case, risking the possibility that there will be no proceeds in excess of creditors' claims. Creditors are primarily interested in return of their principal with interest. Even though they also have collectively 96 percent of the equity interest in the reorganized company, they are likely to prefer a quick settlement with the United States to full and fair compensation through litigation.

Conclusion

For the foregoing reasons, a writ of certiorari should issue to review the judgment and order of the United States Court of Appeals for the Third Circuit.

Respectfully submitted,

CLETUS P. LYMAN,
RICHARD A. ASH,
Attorneys for Petitioners.

Lyman & Ash,
1612 Latimer St.,
Philadelphia, PA 19103,
(215) 732-7040.

TEXT OF CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

AMENDMENT V

THE CONSTITUTION OF THE UNITED STATES

"No person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

Relevant Provisions
of
SECTION 77, BANKRUPTCY ACT

Reproduced in the appendix at 20a-21a.

SECTION 356, CHAPTER XI, BANKRUPTCY ACT

"An arrangement within the meaning of this chapter shall include provisions modifying or altering the rights of unsecured creditors generally or of some class of them, upon any terms or for any consideration."

SECTIONS OF THE PENNSYLVANIA BUSINESS CORPORATION LAW,
15 P.S. §§ 1311 AND 2102
(§ 1320(1) is reproduced in
the appendix at 33a).

§ 1311. Voluntary transfer of corporate assets

* * *

B. A sale, lease, or exchange of all, or substantially all, the property and assets, with or without the good will of a corporation, whether to a subsidiary corporation or not, if made neither (1) in the usual and regular course of its business, nor (2) for the purpose of relocating the business of

the corporation, nor (3) in connection with its dissolution or liquidation, may be made upon such terms and conditions and for such considerations which may consist, in whole or in part, of money or property, real or personal, including shares, or bonds, or other evidences of indebtedness of any other corporation, domestic or foreign, as may be authorized in the manner hereinafter provided in this subsection. The board of directors shall adopt a resolution recommending such sale, lease or exchange, and directing the submission thereof, to a vote of the shareholders entitled to vote in respect thereof at a meeting which may be either an annual meeting of the shareholders or a special meeting of the shareholders entitled to vote in respect of such sale, lease, or exchange. Written notice stating that the purpose, or one of the purposes, of such meeting is to consider the sale, lease, or exchange of all, or substantially all, the property and assets of the corporation, shall be given to each shareholder of record, whether or not entitled to vote, at least ten days prior to the date of the meeting, in the manner provided by this act for the giving of notice of meetings of shareholders. If such meeting be an annual meeting, such purpose may be included in the notice of the annual meeting. * * * At such meeting, the shareholders may authorize such sale, lease, or exchange, and fix or may authorize the board of directors to fix, any or all of the terms and conditions thereof, and the consideration to be received by the corporation therefor. Such authorization shall receive the affirmative vote of the shareholders entitled to cast at least a majority of the votes which all shareholders are entitled to cast on the question, and if any class of shares is entitled to vote as a class on the question, the affirmative vote of the holders of at least a majority of the outstanding shares of each class of shares entitled to vote as a class.

* * *

§ 2102. Election of corporation to dissolve voluntarily

Any business corporation which has commenced business and which has issued shares may elect to dissolve voluntarily, and wind up its affairs, by a written agreement signed by all the shareholders of record of the corporation consenting to its dissolution, or after the board of directors shall have adopted a resolution recommending that the corporation be dissolved voluntarily, and directing that the question of dissolution be submitted to a vote of the shareholders at a meeting which may be either an annual meeting of the shareholders, or a special meeting of the shareholders entitled to vote on the question. Written notice, stating that the purpose, or one of the purposes, of such meeting is to discuss the advisability of voluntarily dissolving the corporation, shall be given to each shareholder of record, whether or not entitled to vote, within the time and in the manner provided in this act for the giving of notice of meetings of shareholders. If such meeting be an annual meeting, such purpose may be included in the notice of the annual meeting. The resolution shall be declared adopted upon receiving the affirmative vote of the shareholders entitled to cast at least a majority of the votes which all shareholders are entitled to cast on the resolution, and if any class of shares is entitled to vote on the resolution as a class, the affirmative vote of the holders of at least a majority of the outstanding shares of each class of shares entitled to vote on the resolution as a class.